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MICHAEL RODAK, JR., C

IN THE

Supreme Court of the United States

OCTOBER TERM, 1972

72-159

RALPH COX, JR. & AIR TRADEWAYS,
Petitioners-Defendants,

v.

WALTER E. HELLER & COMPANY, INC.,
Respondent-Plaintiff.

PETITION OF WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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SUBJECT INDEX

	Page
Opinions Below	1
Issue for Review: FRCP Rule 41-(b) Application	2
Statement of the Case: Nature of Action, Proceedings and Determination	2
Facts Relevant to Certiorari	3
Argument in Support of Certiorari	7
Conclusion	12
Appendix A	13
Appendix B	33

TABLE OF AUTHORITIES CITED

CASES

Bernhardt v. Polygraphic Co. of America, Inc., 350 U.S. 198, 100 L. ed. 199, 76 S. Ct. 273	10
Byrd v. Blue Ridge Rural Electric Cooperative, Inc. (356 U.S. 525, 2 L. ed.2d 953, 78 S. Ct. 893; May 19, 1958)	9
Cage v. Cage, 74 F.2d 377	11
Guaranty Trust Co. v. York, 326 U.S. 99, 108, 89 L. ed. 2079, 2085, 65 S. Ct. 1464, 160 ALR 1231	10
Krause v. Mississippi Coal Corp., 93 F.2d 515	11
Larsen v. O'Reilly, 11 F.R.D. 604 (S.D.N.Y.1951)	9
Pueblo de Taos v. Archuleta, 64 F.2d 807	11
Woodward v. White Satin Mills Corp., 42 F.2d 987	11

RULES

Federal Rules of Civil Procedure, Rule 41(b)	2, 7, 9, 10, 11, 12
Federal Rules of Civil Procedure, Rule 41(c)	7
Federal Rules of Civil Procedure, 28 U.S.C. 2072	11

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PETITION OF WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

The petitioners Ralph Cox, Jr., and Ocean Air Tradeways respectfully pray that a writ of certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Second Circuit entered in this cause on February 26, 1973.

OPINIONS BELOW

Honorable Arnold Bauman, Judge, of the United States Court in the Southern District of New York entered judgment in this cause on June 5, 1972 against Ralph Cox, Jr. and Ocean Air Tradeways,

a partnership. Judge Bauman's opinion is reported at 343 Fed. Supp. 519. Both defendants appealed and the Second Circuit Court of Appeals affirmed, on February 26, 1973, adopting the trial court's opinion which is fully set forth in "Appendix A" to this petition.

ISSUE FOR REVIEW

FRCP RULE 41-(b) APPLICATION

Is it error for a trial court to disregard all uncontroverted evidence of another court's actual intent and to substitute therefore a dogmatic, *substantive* application of Rule 41(b) of the Federal Rules of Civil Procedure, when Rule 41(b) effects a different ultimate result than state law when applied to the same point?

STATEMENT OF THE CASE

NATURE OF ACTION, PROCEEDINGS AND DETERMINATION

This appeal arises from an action to enforce contracts of guaranty on a loan made to a third party. Federal jurisdiction in the matter is based upon the diversity of citizenship of the parties. Litigation was commenced against one of the defendant-petitioners in the U. S. District Court in the District of New Jersey. The other defendant-petitioner was sued in the U. S. District Court in the Southern District of New York. The action commenced in New Jersey was by stipulation ordered transferred to the South-

ern District of New York. The cases were subsequently consolidated for all purposes.

The consolidated cases were brought to trial on January 24, 1972. After ten days of trial the court took the matter under advisement. One hundred and ten days later, the court entered its findings in favor of the respondent. Ten days later, on June 5, 1972 judgment was entered against the petitioners in the sum of $166,017.44. From that judgment, both defendants appealed. Judgment was affirmed by the Second Circuit Court of Appeals on February 26, 1973.

FACTS RELEVANT TO CERTIORARI

Document numbers and page references are to the Record on Appeal before the Second Circuit; exhibit numbers from trial court.

The plaintiff-respondent Walter E. Heller & Company loaned $1,700,000.00 to United States Overseas Airlines on November 23, 1962. Conracts of guaranty were given to plaintiff by Ralph Cox, Jr., and Ocean Air Tradeways, a partnership, the defendants-petitioners herein (Document 19, pp. 1, 2). The plaintiff company has collected approximately $2,100.000.00 toward retirement of the $1,700,000.00 loan (Pl.'s Exh. 43).

The debt to Heller was evidenced by a promissory note by U.S.O.A. providing monthly installments. Interest at the rate of 12½% per annum was added to the principal and the note was made in the face amount of $1,979,631.75 with 24 monthly install-

ments of $69,000.00 each and a twenty-fifth final installment of $323,631.75 (Document #19, p. 2).

U.S.O.A. failed to make the first five installments when they became due. Through various means, including sales of collateral ordered by the Heller company, payments were made that exceeded the amounts of principal and interest then due Heller under the terms of the note. As of February, 1964, the monies collected by Heller exceeded the payments called for by the note by over $450,000.00 (Document #31, p. 393). Payments in advance of their due dates were made under threat of the declaration of a prior default (Document #35, p. 965). Advance collections impaired the working capital position of U.S.O.A. (Document #34, p. 857) and in July, 1965, the company was in default again when the $323,631.75 final installment came due (Document #34, p. 916).

The Heller company declared a default in July, 1965, and proceeded to enforce its contract rights against collateral (Document #34, p. 916).

U.S.O.A. filed a petition under Chapter 11 of the Bankruptcy Act in September, 1966, in the District of New Jersey. The Heller company filed a petition with that court asserting the priority of its chattel mortgage lien against all physical assets of the bankrupt and seeking permission to sell property then in possession of the trustee. The Referee entertained evidence on the amount of the debt claimed by Heller.

Subject to later determination of certain counterclaims asserted against Heller, the Referee entered an order allowing Heller to proceed with the proposed sale (Plaintiff's Exhibit 8). Under the permission of that order, the proposed sale was held on May 4, 1967.

After the sale, a date was set for the presentment of evidence on the counterclaims. For various attributable to the convenience of the parties and the court, the matter was adjourned and re-set several times. On August 28, 1967, the Referee called the matter for hearing. Mr. William Doherty of the New Jersey bar announced that his principal witness was out of the state assisting in the care of his invalid mother who was hospitalized at that time (Document #33, p. 663).

After discussing those facts, and inquiring of counsel for the Walter E. Heller Company as to the availability of his client for service of process in an action that might be commenced in a court of plenary jurisdiction on behalf of the trustee in the bankruptcy proceeding, the Referee entered an order dismissing the counterclaims.

The Referee did not expressly state that the dismissal was without prejudice, but he absolutely evidenced that as his intent to counsel in the courtroom at the time. Counsel for the debtor corporation wrote his client the following day, advising that the order of dismissal was "without prejudice to the Trustee"

maintaining an action thereon (Document #33, pp. 641-642).

Counsel for the Heller Company prepared the order of dismissal and submitted it to Referee Lipkin for signature without first procuring Mr. Doherty's approval as to its form (Document #33, pp. 697-8). The order merely stated that the counterclaims were dismissed and did not specify whether it was with, or without, prejudice (Pl.'s Exhibit 11).

The New Jersey rules provide that such an order of dismissal is not prejudicial unless it expressly provides that it is intended to be (Document #33, p. 703).

The Heller company's appearance before the bankruptcy Court was under an express reservation as to limitation of jurisdiction (Document #33, pp. 639-40).

In his decision here Judge Bauman ruled that the semantic impact of FRCP 41(b) precludes consideration of uncontradicted extrinsic evidence bearing on the court's actual intent upon the entry of an order of dismissal (Document #19, p. 7). *Appendix A.*

The defendant Ralph Cox, Jr. was a member of the defendant partnership Ocean Air Tradeways. He was also a principal shareholder and President of United States Overseas Airlines, and in that capacity

assisted in maintenance of the debtor's position in the bankruptcy proceedings before Referee Lipkin.

Judge Bauman found that Mr. Cox's participation and interest in the bankruptcy proceedings put the Ocean Air Tradeways partnership in privity with the debtor corporation, and that such privity extended the res judicata effect of the ultimate facts found by that court to the present action (Document #19, pp. 8-9).

ARGUMENT IN SUPPORT OF CERTIORARI

Is it error for a trial court to disregard all uncontroverted evidence of another court's actual intent and to substitute therefor a dogmatic, *substantive* application of Rule 41(b) of the Federal Rules of Civil Procedure, when Rule 41(b) effects a different ultimate result than state law when applied to the same point?

FRCP 41 (b) and (c) provide:

> (b) INVOLUNTARY DISMISSAL: EFFECT THEREOF. For failure of the plaintiff to prosecute or to comply with these rules or any order of court, a defendant may move for dismissal of an action or of any claim against him. After the plaintiff has completed the presentation of his evidence, the defendant, without waiving his right to offer evidence in the event the motion is not granted, may move for a dismissal on the ground that upon

the facts and the law the plaintiff has shown no right to relief. *Unless the court in its order for dismissal otherwise specifies, a dismissal under this subdivision and any dismissal not provided for in this rule, other than a dismissal for lack of jurisdiction or for improper venue, operates as an adjudication upon the merits.* (Emphasis supplied.)

(c) DISMISSAL OF COUNTERCLAIM, CROSS-CLAIM, OR THIRD-PARTY CLAIM. The provisions of this rule apply to the dismissal of any counterclaim, cross-claim, or third-party claim. A voluntary dismissal by the claimant alone pursuant to paragraph (1) of subdivision (a) of this rule shall be made before a responsive pleading is served or, if there is none, before the introduction of evidence at the trial or hearing.

Upon trial of this matter, William Doherty, Esquire, duly sworn, testified that the Referee in bankruptcy intended to dismiss certain counterclaims without prejudice (Document #33, p. 641). At the time of the dismissal, the Referee made inquiry of counsel for the Heller Company as to the availability of his client for service of process for the Trustee's pursuit of the counterclaims at a later date (Document #33, pp. 639-642a).

A germane excerpt from Mr. Doherty's testimony is set forth in "Appendix B" to this petition.

Mr. Doherty further testified that he wrote the president of the debtor corporation, on the day after the hearing in which the dismissal was ordered, and advised him of the action by the court. In that letter he explained that the dismissal was without prejudice to the rights of the Trustee pursuing the counterclaims at a later date (Document #33, p. 641).

Judge Bauman committed clear error when he disregarded the foregoing uncontradicted evidence on the intended nature of Judge Lipkin's order of dismissal.

Instead of considering the competent evidence brought to bear on the point, Judge Bauman applied a dogmatic substantive interpretation of FRCP 41 (b), and held that the order was entered with prejudice. In support of his holding in that regard he cited the case *Larsen* v. *O'Reilly*, 11 F.R.D. 604 (S.D.N.Y. 1951).

Mr. Justice Brennan of the United States Supreme Court, in its majority opinion in *Byrd* v. *Blue Ridge Rural Electric Cooperative, Inc.* (356 U.S. 525, 2 L. ed.2d 953, 78 S. Ct. 893; May 19, 1958), reasoned: "*. . . cases following Erie [Railroad* v. *Tomkins] have evinced a broader policy to the effect that the federal courts should conform as near as may be—in the absence of other considerations—to state rules even of form and mode where the state rules may bear substantially on the question whether the litigation*

would come out one way in the federal court and another way in the state court if the federal court failed to apply a particular local rule." In support of the basic rationale, Justice Brennan cited *Guaranty Trust Co.* v. *York*, 326 U.S. 99, 108, 89 L. ed. 2079, 2085, 65 S. Ct. 1464, 160 ALR 1231, and *Bernhardt* v. *Polygraphic Co. of America, Inc.*, 350 U.S. 198, 100 L. ed. 199, 76 S. Ct. 273.

The legislative authorization for the promulgation of the Federal Rules of Civil Procedure expressly limits the authority delegated to this court to *procedural* effect. Under present decisional interpretation, the impact of FRCP 41 (b) is *substantive*. The enactment of the rule changed the law and effectively deprives the petitioners of their most fundamental due process right of a day in court on the merits of their cause.[1]

Cases bearing on application of sections of the equity codes which pre-date enactment of modern FRCP 41 (b) have held that a decree dismissing for want of prosecution, which shows on its face the ground of dismissal, is no bar to a subsequent action,

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[1]Because of the limited review of FRCP 41 (b) by appellate courts, we have found no case law directly in point with the situation set forth in his proposition.

In all available authority, we have found inadequate background history to be of benefit to this court in its determination of this question.

The notes of the advisory committee for the adoption of the significant language in the rule were ordered impounded by Chief Justice Fred M. Vinson on November 10, 1952, and thereafter the order was reaffirmed by the succeeding Chief Justices. That order dictates present policy of the Administrative Office of the United States Courts where the records are impounded.

Mr. Carl Imlay, General Counsel to the Administrative Office referred to the Chief Justice's order in explaining to Steward R. Carter, Jr., Esquire, that the records are not available to the public, when he made inquiry there for the purpose of research on this appeal. Therefore, except by order of this court, there is no "legislative history" available as authority on the question presented.

and is not erroneous for failure to include the words "without prejudice". *Krause* v. *Mississippi Coal Corp.*, 93 F.2d 515. A dismissal for failure to prosecute should be without prejudice. *Cage* v. *Cage*, 74 F.2d 377.

Judge McDermott of the 10th Circuit Court of Appeals, in the 1933 case of *Pueblo de Taos* v. *Archuleta*, 64 F.2d 807, stated that as a general rule dismissal of a cause of action for want of prosecution is not an adjudication of the controversy so as to bar a subsequent suit on the same cause of action.

Historically in American law, a *procedural* rule such as FRCP 41 (b) has been construed so as to distinguish from purely substantive effect. Such a provision in the Equity Code was given the status of a rebuttable presumption. In *Woodward* v. *White Satin Mills Corp.*, 42 F.2d 987, the court held that although dismissal without more is presumed to be a dismissal on the merits, the record may be examined *on appeal* to ascertain what the fact is.

Petitioners urge recognition of the present validity of the rationale of the foregoing theory that FRCP 41 (b) raises a *rebuttable presumption* as to the effect of orders of dismissal. The authority for promulgation of the Federal Rules of Civil Procedure, 28 U.S.C. 2072, extends to the judicial branch of our government a *limited* legislative function for the creation of rules of *procedure*. In part, the second paragraph

provides that *"Such rules shall not abridge, enlarge or modify any substantive right . . ."*

Under the dogmatic semantic connotation applied to FRCP 41 (b) in the instant case, application of the rule can only result in a substantive effect; and therefore would exceed the limits of the enabling authority.

CONCLUSION

In the interest of justice and for the foregoing reasons this petition for a writ of certiorari should be granted.

Respectfully submitted,

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May 24, 1973

APPENDIX

APPENDIX A

WALTER E. HELLER & COMPANY, INC.,
Plaintiff

v.

RALPH COX, JR.,
Defendant.

WALTER E. HELLER & COMPANY, INC.,
Plaintiff,

v.

OCEAN AIR TRADEWAYS, a partnership,
Defendant.

No. 66 Civ. 1437

UNITED STATES DISTRICT COURT
S. D. NEW YORK

May 23, 1972

343 Fed. Supp. 519

BAUMAN, District Judge.

In these consolidated actions plaintiff Walter E. Heller & Company, Inc. ("Heller") seeks to recover upon guaranties executed by defendants Ralph Cox, Jr. ("Cox") and Ocean Air Tradeways ("OAT") respectively, in connection with a $1.7 million loan made by Heller to United States Overseas Airlines, Inc. ("USOA") in November, 1962.

Plaintiff is a Delaware corporation which has its principal place of business in Illinois and does busi-

ness in New York. Since neither defendant is a citizen of New York, Delaware or Illinois, and the amount in controversy exceeds $10,000, this Court has jurisdiction of these actions under 28 U.S.C. § 1332.

It is plaintiff's position that the defendants, by virtue of their respective guaranties, jointly and severally owe to plaintiff, as of January 22, 1972, the sum of $166,017.44.

The defendants, on the other hand, while not denying the execution of the guaranties in question, challenge the validity of the agreements and the extent, if any, of their outstanding liability to plaintiff.

The background of this controversy is as follows: On November 28, 1962, plaintiff entered into a written loan agreement with USOA and various affiliated companies and persons, including Air Power Overhaul, Inc., Ocean Air Tradeways, Inc., Canamex Corporation, and defendants COX and OAT. The loan agreement provided that plaintiff would lend $1,700,000 to USOA and that USOA would repay the loan plus pre-computed interest of $279,631.75 in 24 successive monthly installments of $69,000 each, beginning January, 1963, and a twenty-fifth installment of $323,631.75.

At the time of the loan, USOA executed a collateral installment note in the face amount of $1,979,631.75 reflecting the advance of the $1,700,000 plus

interest. As security for the repayment of this indebtedness, USOA and each of the other parties to the loan agreement executed various instruments, including chattel mortgages and a deed of trust in favor of plaintiff.[1] In addition to requiring repayment of the principal sum of the loan with interest, the note provided for the payment of 12½% interest on each and every payment not timely made. The note also provided that in the event of default, USOA would pay all "exchange and collection charges and a reasonable sum as attorneys' fees if placed in the hands of an attorney for collection."

Contemporaneously with the making of the loan and the execution of the note, and in order to assist USOA in obtaining the Heller financing, defendants Cox and OAT executed and delivered to plaintiff their respective guaranties by which they each guaranteed:

> "* * * the prompt payment in full * * * of any and all indebtedness, obligations and liabilities of every kind or nature (both principal and interest) * * * owing to [plaintiff] by

1. Contemporaneously with the execution of the loan agreement and note, USOA and its various affiliated companies executed and delivered to plaintiff as security for all USOA indebtedness to plaintiff the following security instruments:
(a) A chattel mortgage by USOA to plaintiff covering 14 airplanes and all USOA's machinery and equipment at Cape May County Airport, Wildwood, New Jersey.
(b) A chattel mortgage by USOA, defendant OAT and Canamex to plaintiff covering 69 airplane engines.
(c) A chattel mortgage by Air Power to plaintiff covering Air Power's machinery and equipment located in San Leandro, California.
(d) A chattel mortgage by Canamex to plaintiff covering one airplane.
(e) A chattel mortgage by defendant OAT to plaintiff covering one airplane.
(f) A deed of trust by OAT, Inc. covering approximately 5 acres of land and buildings thereon located at Oakland, California.

> [USOA] * * * and all expenses, collection charges, court costs and attorneys' fees incurred in endeavoring to collect or enforce any of the foregoing against [USOA] and/or [defendants] or any other person or concern liable thereon * *."

In addition, each defendant specifically waived all notice and rights with respect to the indebtedness and collateral to which guarantors are otherwise entitled.

USOA was in default under the loan agreement and note from the outset. The first installment of the loan was only partially paid, and thereafter not one installment was paid in its proper amount or when due. Nonetheless, Heller refrained from declaring a default until July, 1965. At that time, Heller accelerated the entire outstanding debt and began pursuit of collection by, among other things, the sale of collateral.

These sales however, were interrupted when USOA filed an application for an arrangement pursuant to Chapter XI of the Federal Bankruptcy Act in the District of New Jersey. Plaintiff then filed a Notice of Motion and Petition for leave to sell certain assets of USOA which were covered by the chattel mortgages. USOA, at the instigation and direction of Cox and OAT (acting by and through Cox), and with the financial support of OAT, challenged plaintiff's right to conduct the sales and opened a full-scale at-

tack on the validity of the indebtedness. Hearings were held before Referee Lipkin in November, 1966. Heller's Executive Vice President, Edmund Duncan, testified at length to all the relevant facts surrounding the loan and the status of the indebtdeness as of November 15, 1966. The loan agreement, the collateral installment note, chattel mortgages, ledger cards checks and correspondence were submitted in support of Heller's claim. Additionally, a large volume of documents was requested by and produced to counsel for USOA who then undertook a vigorous and extensive cross-examination of Duncan. Among other things, with the direct participation of Cox who was present throughout, he raised questions concerning the propriety of prior sales of collateral, the accuracy of plaintiff's computation of the outstanding indebtedness, the reasonableness of attorney's fees, the computation of interest, and a myriad of alleged improprieties by plaintiff. Every relevant transaction and every item of indebtedness then outstanding was subjected to scrutiny and challenge.

In connection with these proceedings, counsel for USOA propounded interrogatories to plaintiff requesting further information concerning defenses and counterclaims which were allegedly available to USOA. These interrogatories covered the negotiation and closing of the loan, payments made, the existence, condition, ownership and location of collateral, plaintiff's relationship and dealings with Twentieth Century Aircraft, prior sales of collateral by plaintiff, and

plaintiff's actions with respect to the DC-4 aircraft N-90428. Plaintiff was required to and did answer the interrogatories, and a substantial volume of still additional documents were produced.

On January 18, 1967, Referee Lipkin rendered his "Findings of Fact, Conclusions of Law and Order" holding plaintiff's claim valid and establishing a lien in favor of plaintiff, as of November 15, 1966 (the date upon which testimony was commenced), in the amount of $152,232.07.

On March 15, 1967, Referee Lipkin entered an Order granting plaintiff's request to proceed with the sale of USOA's assets in Wildwood, New Jersey. This Order however, was entered without prejudice to USOA's right to assert counterclaims.

Several months after the Court's Order, USOA, on Cox's affidavit, sought to interpose certain counterclaims against Heller in the bankruptcy court as did OAT. They ranged from charges of mismanagement of collateral to usury and fraud. Referee Lipkin permitted the submission of the counterclaims and Heller responded in full. Thereafter, Cox failed on several occasions to appear for a trial of the counterclaims despite specific directions by Referee Lipkin. Finally, he dismissed them.

When Heller completed the sale of the major items of USOA collateral at a publicly held, well publicized,

and well attended auction sale, a substantial deficiency remained. Accordingly, Heller brought these actions against defendants as guarantors of the USOA obligations.

After considering much of the evidence adduced at trial and the memoranda submitted by the parties, this Court made a preliminary determination that Referee Lipkin's Order adjudicating the validity of plaintiff's claim against USOA and his Order dismissing the counterclaims against Heller constituted final judgments against USOA which are *res judicata* in the present actions and conclusively bind each of the defendants as to (a) the question of the validity of Heller's loan, (b) any defenses now raised by defendants based on acts which allegedly occurred prior to November 15, 1966, and (c) the validity and extent of all charges made prior to November 15, 1966. Accordingly, the Court limited the trial to charges and credits since that day. In addition, defendants were permitted to raise defenses not asserted before Referee Lipkin.

The discussion which follows is intended to explain the preliminary determination of this Court and to resolve the questions which were tried to the Court.

I.

As is well known, the legal prerequisites to the application of the doctrine of *res judicata* are: (1) the

existence of a final judgment rendered on the merits, (2) a subsequent action between the same parties or those in privity with them, and (3) the presence of the same claim or demand. See, e.g., *Baltimore Steamship Co.* v. *Phillips*, 274 U.S. 316, 47 S.Ct. 600, 71 L.Ed. 774 (1927); *Saylor* v. *Lindsley*, 391 F.2d 965 (2d Cir. 1968); In re *Weisbrod & Hess Corp.*, 129 F.2d 114 (3d Cir. 1942). If these elements conjoin, the doctrine of *res judicata* operates to bind the parties both as to issues actually litigated and determined in the first suit, and those which might have been, but were not raised and decided. *Cromwell* v. *County of Sac*, 94 U.S. 351, 24 L.Ed. 195 (1877); *Commissioner of Internal Revenue* v. *Sunnen*, 333 U.S. 591, 68 S.Ct. 715, 92 L.Ed. 898 (1948).

(1) Prior Final Judgment on the Merits

The law is settled that the judgment of a Referee in Bankruptcy with respect to a creditor's claim for money or for property is a final judgment and should be given the same effect as any other judgment of a competent court, in a subsequent suit against the bankrupt or any one in privity with him. See, e. g., *Katchen* v. *Landy*, 382 U.S. 323, 86 S.Ct. 467, 15 L.Ed.2d 391 (1966); *Lesser* v. *Gray*, 236 U.S. 70, 35 S.Ct. 227, 59 L.Ed. 471 (1915); In re *Weisbrod & Hess Corp., supra; United States* v. *American Surety Co.*, 56 F.2d 734 (2d Cir. 1932); *United States* v. *Coast Wineries, Inc.*, 131 F.2d 643 (9th Cir. 1942).

It is equally well settled that a dismissal for want of prosecution—unless explicitly provided to be without prejudice—is "with prejudice" and operates as an adjudication on the merits. Federal Rules of Civil Prcedure 41(b) and (c); *Larsen* v. *O'Reilly*, 11 F.R.D. 604 (S.D.N.Y.1951). That is the case here.

(2) The Same Parties or those in Privity with them

The privity of interest necessary to bind a party to the results of a prior proceeding to which he was not a named party can be established in a number of ways. Thus, it is established when it is shown that the defendant in the subsequent action was an officer, director or the major shareholder of the corporate party in the first action. *Towle* v. *Boing Airline Co.*, 364 F.2d 590 (8th Cir. 1966); *Hyman* v. *Regenstein*, 258 F.2d 502 (5th Cir. 1958); cert. denied sub nom. *Hyman* v. *Continental Illinois National Bank*, 359 U.S. 913, 79 S.Ct. 589, 3 L.Ed.2d 575 (1959); In re *Shea's Will*, 309 N.Y. 605, 132 N.E. 2d 864 (1956). See also 1B Moore's Federal Practice, Para. 0.411 at 1558. It may also be established by showing that the party who is sought to be bound by the first judgment was actually a participant in and controlled the prior litigation. See, e. g., *Bros, Inc.* v. *W. E. Grace Mfg. Co.*, 261 F.2d 428 (5th Cir. 1958); *Ark-Tenn Distributing Corp.* v. *Breidt*, 209 F.2d 359 (3rd Cir. 1954); 1B Moore's Federal Practice, Para. 0.411. Finally, a guarantor is bound by a prior adjudication involving the principal debtor if

the guarantor had notice of and an opportunity to participate in the prior proceeding. See e. g., *Broder* v. *Hartford Acc. & Indem. Co.*, 106 F. Supp. 343 (D.D.C.1952); *Jonas & Naumburg Corp.* v. *Michlin*, 220 App.Div. 649, 22 N.Y.S. 442 (1st Dep't. 1927); *Blanding* v. *Cohen*, 101 App.Div. 442, 92 N.Y.S. 93 (1st Dep't. 1905) aff'd. 184 N.Y. 538, 76 N.E. 1089. Cf. *Frederick* v. *United States*, 386 F.2d 481 (5th Cir. 1967).

Applying these standards to the defendants it is clear that the necessary privity between each of them and USOA exists.

COX was the principal shareholder (71.33%), president and director of USOA. He was an active participant in, and was in full control of the USOA defense in the Chapter XI proceeding. He not only signed the Chapter XI petition on behalf of USOA, but retained its counsel and helped finance the retention. Finally, he was a guarantor of USOA's indebtedness to Heller, with notice of the proceedings before Referee Lipkin.

OAT was also an active participant in that proceeding. The evidence discloses that OAT helped to finance it and there sought to assert a claim against Heller. Moreover, defendant Cox, as the managing partner of OAT, had its interests very much in mind. The other two OAT partners were respectively, Cox's mother and brother. All were shareholders of USOA

and in the aggregate owned 89.2% of its stock. Not only were the other partners of defendant OAT on notice of the Chapter XI proceedings, but they were consulted by Cox throughout the course of the proceedings. The various settlement negotiations during the course of the proceedings invariably contemplated the release by Heller of any claim against OAT on its guarantee. Under these circumstances, I conclude that not only was OAT on notice of the Chapter XI proceedings, but in fact was an active participant well aware that its liability was inevitably there being determined. Cf. United States v. Webber, 396 F.2d 381 (3d Cir. 1968).

(3) The Same Claim or Demand

This prerequisite for applying the doctrine of *res judicata* merely requires that there be an identity of issues or grounds between the first and the second actions. See e. g., *Wilson Cypress Co.* v. *Atlantic Coast Line R. Co.*, 109 F.2d 623, cert, denied, 310 U.S. 653, 60 S.Ct. 1101, 84 L.Ed. 1418 (1939). Since it is clear that the amount and validity of USOA's indebtedness to Heller was placed in issue by Heller's petition to sell its collateral, there can be no doubt that both the Chapter XI proceeding and the present litigation relate to the same claim or demand. That is not seriously contested.

Thus, since the "Findings" and the order dismissing counterclaims constitute final judgments against

USOA which are *res judicata* in these actions, defendants are accordingly barred from raising anew any questions decided by Referee Lipkin. The defendants are specifically barred from (a) questioning the amount of the USOA indebtedness found to be existing as of November 15, 1966, (b) raising any defenses based on alleged usury, alleged violation of Section 131(1) of the New York Banking Law, McKinney's Consol.Laws. c. 2 or any rule against charging interest on interest, and (c) asserting any claim of discharge of their guaranties based on facts which allegedly existed prior to November 15, 1966, including any claims based on alleged lack of due diligence in the collection of the USOA indebtedness or the preservation of the collateral.

II.

At trial defendants claimed, for the first time, that plaintiff committed a "fraud in the inducement" by misrepresenting to USOA and defendants that a separate guaranty obtained by Heller from Twentieth Century Aircraft ("Twentieth Century") was "the same as" defendants' guaranties except that it was "partial". They claimed that had they known that it was different they would not have executed their guaranties.

The evidence adduced at the trial does not support this contention. Although defendants asserted that they would prove such fraud through Cox and three

other witnesses, only Cox and Frank Donahue testified that a representative of Heller made statements to that effect. Defendants' other witness, Sidney Dickstein, USOA's former counsel, said quite the contrary. He testified that during the loan negotiations plaintiff made clear that the Twentieth Century guaranty was materially different from the one signed by Cox and OAT and corroborated plaintiff's witnesses Duncan and Ruben who testified that Donahue, a "sales manager," had not been privy to the negotiations. Additionally, Duncan and Ruben stated that they personally advised representatives of USOA of the differing nature of the Twentieth Century guaranty prior to the consummation of the loan. Having heard the testimony, I conclude that the defendants were fully notified that this guaranty differed materially from those signed by defendants.

III.

Defendants also claim that after November 15, 1966 Heller failed to properly realize on the collateral and that, as a result, they are released from their obligations. The authorities agree that one who unconditionally guaranties an indebtedness is not released or discharged by virtue of any lack of diligence with respect to, or release or impairment of, collateral by a secured creditor. See e. g., *Nation Wide, Inc.* v. *Scullin*, 256 F.Supp. 929 (D.N.J.1966), aff'd, 377 F.2d 554 (3d Cir. 1967); *United States* v. *Shirman*, 41 F.R.D. 368, 372-73 (1966); *United States* v. *New-*

ton Livestock Auction Market, Inc., 336 F.2d 673 (10th Cir. 1964); *Indianapolis Morris Plan Corp.* v. *Karlen*, 28 N.Y.2d 30, 319 N.Y.S.2d 831, 268, N.E.2d 632 (1971). Here defendants' guaranties are unconditional guaranties of payment. They specifically provide that:

> "[Defendant unconditionally guarantee[s] to [plaintiff] * * * the prompt payment in full at maturity and all times thereafter * * * any and all indebtedness, obligations and liabilities of every kind or nature (both principal and interest) now or at any time hereafter owing to [plaintiff] by [USOA] * * *.
>
> * * * The [defendant] * * * waive(s) notice of any consents to the granting of indulgence or extention of time payment, the taking and releasing of security in respect of any * * agreements, obligations, indebtedness or liabilities so guaranteed hereunder, or [plaintiff's] accepting partial payments thereon or [plaintiff's] settling, compromising or compounding any of the same in such manner and at such times as [plaintiff] may deem advisable, without in any way impairing or affecting [defendant's] liability for the full amount thereof; and [plaintiff] shall not be required to prosecute collection, enforcement or other remedies against the debtor, or against any person liable on any said * * * agreements, obligations, indebtedness or liabilities so guaranteed, or to enforce or resort to any security, liens, collateral or other rights or remedies thereto ap-

> pertaining, before calling on [defendant] for payment; nor shall [defendant's] liability in any way be released or affected by reason of any failure or delay on [plaintiff's] part so to do.
>
> This guaranty is absolute, unconditional and continuing * * *."

In addition, I find that defendants' claim is factually baseless. There has been no credible showing that plaintiff was in any way responsible for any dissipation of value or that any of plaintiff's activities resulted in the realization of anything less than the fair value of the collateral sold. All the evidence is to the contrary and tends to show that plaintiff sought to maximize its receipts from such sales. Plaintiff proved that the sale of collateral at Wildwood was well publicized, well attended and properly conducted. Cox's claim that 30 of his "personal" antique street lamps were improperly sold was specifically contradicted by defendants' own witness, Andrea Lippi.

Similarly, Cox's claim that Heller permitted the deterioration of a DC-4 aircraft (N-90428) located in Miami, Florida was specifically refuted by Dan Cox who testified that the plane was little more than a hulk and was subject to possessory liens for storage and gasoline.

Finally, defendants' claim that Heller improperly dealt with a DC 54 aircraft (N-44994) located in

Oakland, California is wholly unsubstantiated by the record. The evidence shows that the plane was nearly worthless by 1965 when Heller attached it, and that Heller reasonably concluded that its value was not worth the costs that would be expended in pursuing a sale.

IV.

Defendants have claimed that the interest rate on their outstanding indebtedness should be limited to 6% per annum because that was the rate utilized by Referee Lipkin in his Findings of Fact, Conclusions of Law and Order in the Chapter XI proceedings. The agreements involved here, however, obligate the defendants to pay interest at 12½% per annum on all post maturity sums owing under the note and agreement which were guaranteed by defendants. The fact that Referee Lipkin limited the rate for his purposes can have no effect here since his Order was limited to the Chapter XI proceedings.

V.

Defendants also contend that as of February 27, 1964 plaintiff had received total "payments" of $1,434,635.09 ($1,309,635.09 of which represented proceeds of collateral sold by USOA and proceeds of a partial assignment of a claim against the United States), which amounted to more than the first 14 scheduled note installments of $69,000 each. This overpayment, they claim, constituted a modification of the

agreements they guaranteed and they are thereby released from any liability. This defense is without merit.

The loan agreement specifically provides that all proceeds from the sales of collateral by USOA and the assigned Government claim were to be treated as mandatory "prepayments" and, as such, were to be applied to the installments coming due under the note in the inverse order of their maturity unless Heller consented and agreed to some other application. Since the uncontradicted evidence at trial shows that Heller never consented to any other manner of application of these proceeds, USOA made no overpayments. In fact, as of February 27, 1964 USOA had only made actual "payments" totaling $125,000 against the total price of $966,000 that was due on the first 14 monthly installments of $69,000. The proceeds of the sales of collateral and the Government claim, when applied to the installments in their inverse order of maturity, are not sufficient to make up the difference.

Even if the underlying agreement between Heller and USOA had been modified the defendants would not be discharged from their guaranties since they specifically consented to modifications of the relevant agreements by the very terms of their guaranties. Cf., *Indianapolis Morris Plan Corp.* v. *Karlen, supra.* The determinative language of defendants' guaranties is as follows:

"[Defendants] do hereby jointly and severally unconditionally guarantee to [plaintiff] * * * the prompt payment in full at maturity and all times thereafter (waiving notice of nonpayment) of any and all indebtedness, obligations and liabilities of every kind or nature (both principal and interest) now or at any time hereafter owing to [plaintiff] by [USOA] * * * and the prompt, full and faithful performance and discharge by [USOA] of each and every the [sic] terms, conditions, agreements, representations, warranties, guaranties and provisions on the part of [USOA] contained in any such agreement or arrangement *or in any modification or addenda thereto or substitution thereof*, * * *." (Emphasis added)

VI.

Finally, defendants have raised the claim that their guaranties lack consideration. It is settled law that a contract of guaranty entered into concurrently with the principal obligation is supported by the same consideration which underlies the principal contract. See e. g., *Erie County Savings Bank* v. *Coit*, 104 N.Y. 532, 11 N.E. 54 (1887); *Beacon Hold. Corp.* v. *Sparinger*, 256 *App.Div.* 606, 11 N.Y.S.2d 48 (1st Dep't. 1939).

Through the testimony of Duncan, Kimmelman, Mindich and Black, supported by numerous exhibits maintained by plaintiff in the course of its business, plaintiff has established that the guaranteed indebt-

edness sued upon was $166,017.44, as of January 22, 1972.

The various debits to the defendants' account since November 15, 1966—the effective date of Referee Lipkin's Findings of Fact, Conclusions of Law and Order—consist primarily of attorneys fees, insurance costs and expenses of sales of collateral. They were directly related to plaintiff's post-default collection efforts against USOA and the several guarantors including the defendants and I find them reasonable in amount.

Plaintiff has also properly charged the USOA account with interest at the rate of 12½% per annum on all outstanding amounts other than on accrued interest owing to the plaintiff. Plaintiff has credited the USOA account with certain net collections received by plaintiff since November 15, 1966 from sales of collateral. These collections were properly applied by plaintiff first to the reduction of accrued interest and then to the reduction of principal, including plaintiff's costs and expenses of collection. Accordingly, as of January 22, 1972, the outstanding indebtedness owing to plaintiff on the USOA account by defendants pursuant to their respective guaranties was $166,-017.44.

The foregoing shall constitute my findings of fact and conclusions of law in compliance with Rule 52(a) Fed.R. Civ.P.

The parties may submit a judgment in accordance with the opinion herein.

So ordered.

APPENDIX B

(Excerpt from Document 33, pp. 633-641.)

William P. Doherty, Jr., called as a witness on behalf of defendants, being first duly sworn, testified as follows:

Direct examination

By Mr. Smalley:

Q Where do you reside, Mr. Doherty?

A Bridgeton, New Jersey.

Q What is your profession, please?

A I am an attorney.

Q How long have you been actively engaged in the private practice of law?

A 11 years.

Q Mr. Doherty, have you had occasion to represent US Overseas Airlines?

A Yes, in conjunction with David L. Horuvitz with whom I was in practice at the time.

Q Did you make appearances in a court of Judge Lipkin of the Federal Bankruptcy Court in your district in New Jersey?

A Yes, sir.

Q On what matters did you appear before Judge Lipkin on behalf of USOA?

A Prior to the corporation being adjudicated I had appeared before Judge Lipkin—I can't say how many times nor the dates at this point—both formally and informally in his chambers. I would suppose three or four times prior to the adjudication, while it was still in Chapter XI.

Q What were the matters that the court was entertaining on those occasions?

A Well, of course, during the period that a reorganization was contemplated there were various negotiations being had with prospective participants in the plan which, of course, would be communicated to Judge Lipkin for the purpose of securing his thoughts on whether he felt that they would be adequate or not, that type of thing.

There were some continuances on various aspects which I can't recollect particularly and one time I recall appearing before Judge Lipkin on a return date that he had set which had been continued two or three times, for the commencement of litigation on the counterclaims by the debtor at that point against the Heller organization, Heller Factors and Heller & Company.

Q Had the Heller Company denied the jurisdiction of that court for the litigation of those counterclaims?

A That was my understanding.

Q What orders did Judge Lipkin enter and what findings did he make with respect to the counterclaim on that occasion?

A Well, on a number of occasions, I presume three or four, commencing some time in the spring of 1967 as I recall, there had been dates set for the proceeding by the debtor, still a debtor at that point, on the counterclaims. The dates were continued for various reasons.

Finally, a date was set for August 28th.

Mr. Kimmelman had—now Judge Kimmelman—had appeared with me on two or three prior occasions along with people I believe from the Wachtell firm here in New York, Mr. Duncan I believe was there a couple of times.

On August 28th, because Mr. Cox was unable to be there, I appeared as scheduled before Judge Lipkin to apprise him of the situation. Dr. Cox was I believe in Mississippi or some place, had not been able to be there because of the illness of his father and/or mother, I'm not sure which, and the judge was on the record at that point and indicated that he had set the matter down for hearing on that date and stated that the debtor was not present.

Whereupon Mr. Kimmelman made a motion to dismiss. The judge entered an order—I don't know whether it was ever signed—entered an order dismissing the counterclaims.

At that time when Mr. Kimmelman's motion, I believe Mr. Wachtell was there though I am not sure and I think Mr. Duncan was there.

Q What was the effect of that order to you?

The Court: It is pretty obvious, the counterclaims were dismissed, period.

The Witness: No, your Honor, it wasn't that clear-cut, otherwise I wouldn't be here.

Mr. Wachtell: Could we have a proper question because I object to this one.

The Court: Sustained.

Q What facts do you have knowledge of that bear upon the nature of the order entered by Judge Lipkin at that time?

Mr. Wachtell: That is objectionable.

The Court: Let met ask was there an order entered by Judge Lipkin?

The Witness: Yes.

The Court: Is there not a copy of that order in the record?

Mr. Wachtell: Yes, Exhibit 11.

The Court: May I have it please?

(Handed to Court)

The Court: I show you Exhibit 11 for identification and ask you if that is a copy of the order that Judge Lipkin signed.

The Witness: Your Honor, it appears to be. What I have is a copy as it was forwarded to the judge. I have never received a conformed copy. However, the date of the filing—

The Court: And the signature on the second page?

The Witness: It appears to be the same order.

The Court: Let us asume that is Judge Lipkin's order, right?

The Witness: I am satisfied.

The Court: Now, ask a question, Mr. Smalley.

Q Do you have knowledge of facts bearing upon the effect of that order by Judge Lipkin?

The Court: What do you mean the effect?

Q The intended effect by Judge Lipkin.

Mr. Wachtell: I object to the question, your Honor. There is a question whether anything was said.

The Court: I am coming to that, Mr. Wachtell.

Mr. Wachtell: Then my only objection would be an attempt to impeach a prior order.

The Court: Was anything said in connection with the issuance of this order at that time or about the time it was signed by Judge Lipkin or anybody in Mr. Lipkin's presence?

The Witness: Your Honor, at about the time it was signed—I don't know, I am not aware that it was signed that day or the day after. Apparently the argument—

The Court: It seems to be dated the 29th of August, 1967.

The Witness: As I understand the argument and the order were entered orally on the 28th, your Honor.

The Court: What was said at the time that Referee Lipkin indicated his decision?

The Witness: Very well. I requested from Judge Lipkin to indicate on the record whether this order was being entered with or without prejudice.

In New Jersey it is very, very unusual to have an order entered merely dismissing a matter. In fact, our rules provide, our New Jersey rules provide that an order entered merely of dismissal is in fact without prejudice. So I was unused to having orders entered without a designation of with or without prejudice.

So I asked Judge Lipkin once or twice or two or three times perhaps to specify whether he meant with or without prejudice because at that point we were concerned about the course we would follow procedurally and if it was with prejudice I would be in a position to appeal. If it were without prejudice then our relief would be otherwise.

Judge Lipkin did not specify with or without prejudice specifically. However, he did say or he asked Mr. Kimmelman my recollection is can Heller be found anywhere in the—the problem was Heller was not officially in the jurisdiction as far as I was concerned because of the caveat under which they entered the litigation and therefore if we were to have preserved our right of action against Heller, and the corporation was not under the jurisdiction of the New Jersey courts or finable in New Jersey, that we might not be able to sue them there, we might have to come to New York or Chicago or some place else.

So Judge Lipkin asked Mr. Kimmelman is Heller available for suit, meaning can he be served and my

recollection was that either Mr. Kimmelman indicated that he was, it was servable through the corporation trust or Prentice Hall or service or they had a registered agent in New Jersey and the judge indicated that, well, if we were to pursue our claim subsequent to this action in another action, that the inquiry was made of Mr. Kimmelman, somewhat jocularly obviously that well, suppose they get a judgment against Heller, is it judgment proof. Obviously that particularly I recollect.

Of course, to state the question is to answer it, they are not judgment proof and so far as I was concerned the debtor could try again in another court. I received a copy of Irving Kimmelman's letter dated August 28, 1967, the same date as the hearing which he apparently had with him at the time anticipating a result or went back to Newark and mailed from his office which I presume is what happened, wherein he transmitted to Judge Lipkin an original and two copies of an order in conformity with your Honor's ruling this morning—reading from the letter, and Mr. Kimmelman forwarded to me with that a copy of the draft of Exhibit No. 11, unsigned, of course.

When I got that I wrote to Dr. Cox and I believe I had spoken to him on the telephone in the meantime, and in the letter, if your Honor wishes to hear, I say you will note that the counterclaims were dismissed without prejudice to the trustee proceeding to prosecute same if he finds there is merit in same.

On August 28th it is my recollection that Judge Lipkin adjudicated the corporation a bankrupt so anything thereafter had to be done by the trustee.

I have absolutely no reservation about saying that the colloquy as it was, Judge Lipkin clearly indicated this order was without prejudice, your Honor.

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MICHAEL RODAK, JR.,

IN THE

Supreme Court of the United States

OCTOBER TERM, 1972

No. 72-1595

RALPH COX, JR., AND OCEAN AIR TRADEWAYS,

Petitioners,

v.

WALTER E. HELLER & COMPANY, INC.,

Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO THE PETITION FOR WRIT OF CERTIORARI

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June 21, 1973

INDEX

	PAGE
Opinions Below	1
Jurisdiction	1
Question Presented	2
Statute Involved	2
Statement of the Case	2
Argument	8
I. The Decision Below is Clearly Correct	9
II. The Petition Does Not Raise Any Issue Requiring Review By This Court	13
Conclusion	14

CITATIONS

Cases:

American Nat. Bank & Trust Co. of Chicago v. *United States*, 142 F.2d 571 (D.C. Cir. 1944) 9, 10, 11

Broder v. *Hartford Acc. & Indemnity Co.*, 106 F. Supp. 343 (D.D.C. 1952) 9

Byrd v. *Blue Ridge Rural Electric Cooperative, Inc.*, 356 U.S. 525 13

Erie R. Co. v. *Tompkins*, 304 U.S. 64 13

Fischer v. *Dover S.S. Co.*, 121 F. Supp. 528 (E.D.N.Y. 1954) 9

Hanna v. *Plumer*, 380 U.S. 460 ..... 12, 13

Hicks v. *Bekins Moving & Storage Co.*, 115 F.2d 406 (9th Cir. 1940) 9

PAGE

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Weissinger v. *United States*, 423 F.2d 795 (5th Cir. 1970) 9, 10

Statutes and Rules:

Federal Rules of Civil Procedure:

Rule 41(b) 2, 5, 6, 8, 9, 10, 11, 12, 14

Rule 41(c) 2, 6, 9

General Orders in Bankruptcy:

Order 37 12

New Jersey Civil Rules:

Section 1:2-4 12

Section 4:37-2(d) 12

Section 4:42-2(b) 12

Other Authorities:

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In the

Supreme Court of the United States

OCTOBER TERM, 1972

No. 72-1595

Ralph Cox, Jr., and Ocean Air Tradeways,

Petitioners,

v.

Walter E. Heller & Company, Inc.,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF RESPONDENT IN OPPOSITION

Opinions Below

The Opinions below are adequately set forth in the Petition.

Jurisdiction

The jurisdiction below was based upon diversity of citizenship (28 United States Code § 1332).

Question Presented

Is it error for a Federal District Court to hold that a Federal Referee in Bankruptcy's order of dismissal, which did not specify that the order was entered *without* prejudice, was a dismissal *with* prejudice where: (a) Rules 41(b) and (c) of the Federal Rules of Civil Procedure expressly state that such an order of dismissal, other than upon grounds not relevant herein, is *with* prejudice unless otherwise specified; (b) the Bankruptcy Court is subject only to the Federal Rules of Civil Procedure; (c) the testimony offered by the parties attacking the order established that the Referee in Bankruptcy never stated the dismissal was without prejudice; and (d) the Referee in Bankruptcy subsequently issued an opinion flatly stating that the order of dismissal was intended to be *with* prejudice?

Statute Involved

The pertinent provisions of Rules 41(b) and (c) of the Federal Rules of Civil Procedure are set forth in the Petition at pp. 7-8.

Statement of the Case

This litigation arises from a loan made by respondent to United States Overseas Airlines, Inc. ("USOA"), as to which petitioners had executed contracts of guaranty. In view of the narrow question raised by the petition for certiorari, the history of respondent's dealings with USOA prior to the latter's filing of a petition in bankruptcy may be omitted.

In September, 1966, several months after the institution of this litigation to enforce respondent's rights against petitioner Cox ("Cox") on his guaranty and just as respondent was about to proceed with a substantial sale of

USOA's assets, USOA (through Cox, its president) filed a Chapter XI petition in the federal bankruptcy court for the District of New Jersey (Exh. 1e).*

Shortly after the filing of the Chapter XI petition, respondent, in order to collect on USOA's secured indebtedness, filed a Notice of Motion and Petition for Leave to Sell certain assets of USOA (Exh. 4e). At Cox's personal direction (Doc. 27a, pp. 11-12; 44-45; 51; 63-71; Exh. 9e; 35e; 36e; 101e; 103e; 111e; 113e) and with the advice of all of the other partners of petitioner Ocean Air Tradeways ("OAT") (Doc. 27, pp. 51, 57, 60-61 Doc. 28a, p. 101), USOA proceeded to launch a full scale attack upon both the amount of its indebtedness to respondent and the validity of respondent's lien (Doc. 27a, pp. 9-14; Doc. 37a, pp. 1516-17; Exh. 101e, pp. E-348-49). Respondent was required to prove its lien in full, and thus, at a trial before Referee in Bankruptcy William Lipkin during November and December, 1966, respondent produced substantial documentary and testimonial evidence in support of its petition (Doc. 32a, p. 560; Doc. 33a, p. 596). Counsel for USOA engaged in a vigorous and extensive cross-examination of respondent's executive vice-president in order to establish the invalidity of respondent's claim or to reduce the amount thereof (Doc. 27a, pp. 9-14; Doc. 37a, p. 1516). Among other things, USOA's counsel, with the direct aid and assistance of petitioners Cox and OAT, raised questions concerning alleged prepayment, previous sales of collateral, and various alleged misdeeds by respondent with respect to the guaranteed loan which formed the basis of the present litigation.

On January 17, 1967, after the completion of the aforesaid trial, Referee Lipkin rendered his "Findings of Fact, Conclusions of Law and Order" in which he conclusively

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* References bearing the designation "Exh." and the suffix "e" are to respondent's Appendix of Trial Exhibits in the Court of Appeals. References bearing the designation "Doc." and the suffix letter "a" are to petitioners' Appendix in the Court of Appeals.

adjudicated the validity of respondent's claim and established a lien as of November 15, 1966 (the date upon which testimony had commenced) in the amount of $152,232.07 (Exh. 5e).

Since this indebtedness was the very same indebtedness which was at issue in the present litigation and since petitioners were found to be in complete privity with USOA, the District Court in this proceeding concluded that the aforesaid Findings of Fact, Conclusions of Law and Order were *res judicata* against the petitioners and constituted a bar to any relitigation of the issues thereby determined. Petitioners do not challenge that conclusion in their present petition.

However, the Referee's Order of January 17, 1967 had left open to USOA the opportunity to assert any counterclaims against respondent which might in fact be thereafter shown to exist by virtue of new matter which USOA might thereafter discover by means of written interrogatories which respondent was required to answer in great detail (Exhs. 6e and 7e). On March 31, 1967, USOA, supported by petitioner Cox's affidavit, filed a motion in the Bankruptcy Court for leave to assert extensive counterclaims against respondent seeking damages on behalf of itself and OAT (Exh. 9e). Despite the fact that all of these matters had, or could have, been heard by the Bankruptcy Court in the determination of respondent's lien (Exh. 10e, pp. E-209-212; see also Exh. Ae, pp. E-6-7), Referee Lipkin, desiring to afford USOA the fullest opportunity to be heard, permitted the submission of the counterclaims and required respondent to reply thereto. Respondent submitted a detailed evidentiary response in the form of an affdavit with supporting documentary proof (Exh. 10e). A trial date was thereafter scheduled.

On April 20, 1967, USOA's then designated counsel moved to withdraw from the proceedings (Exh. 34e). An order of the Referee entered May 15, 1967 permitted the withdrawal and required USOA to obtain new counsel by

June 2, 1967 and set the hearing for the trial of its counterclaims for July 11, 1967 (Exh. 35e). On June 13th and again on June 30, 1967, respondent wrote to Cox advising him that, contrary to the order of May 15, 1967, it had not been informed of the retention of new counsel for USOA and that it would move for the dismissal of the counterclaims unless USOA complied with that order (Exh. 103e). On July 11, 1967, the return date of the hearing, USOA still had not retained counsel. The Referee then wrote to petitioner Cox to advise him that the hearing would be adjourned "for a final time" to July 25, 1967, and that if USOA was not ready to proceed on that date, the bankruptcy court would hear respondent's motion to dismiss. Cox ignored this warning and July 25th came and went without either a hearing or the appointment of counsel. On July 26, 1967, new counsel did file a Notice of Appearance for USOA, and the hearing was once again postponed until August 28, 1967.

On August 28, 1967, the newly retained local counsel appeared before Referee Lipkin totally unprepared to proceed with the trial of the counterclaims (Doc. 33a, p. 678; Exh. Ae, p. E-14). In fact, as established by correspondence between new counsel and Cox, these attorneys never agreed to do anything more than serve as local counsel, and neither they nor Cox had ever intended that they would try the case (Exh. 113e; Exh. Ae, p. E-14).*

Frustrated by USOA's continual delay and negligence, Referee Lipkin stated that he would enter an order dismissing the counterclaims, and such an order was entered on August 29, 1967 (Exh. 11e). While this order did not expressly state that the dismissal was with prejudice, the effect of Rule 41(b) of the Federal Rules of Civil Procedure,

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* The above-stated facts clearly belie the statement made by petitioners that their presentment of counterclaims was adjourned and re-set several times "for various [reasons] attributable to the convenience of the parties and the court." (Petition, p. 5).

together with USOA's contumacious refusal to obey the Referee's previous orders to proceed, made it clear that the order was intended to be "with prejudice" and an adjudication on the merits. Accordingly in the District Court below respondent argued, and the Court held, that the Referee's order of dismissal was an additional ground for *res judicata* barring petitioners from asserting the same matters set forth in the dismissed counterclaims.

At the trial petitioners attempted to challenge the foregoing *res judicata* conclusion by arguing that the Referee's order of dismissal should have been deemed to be "without prejudice" and therefore not an adjudication on the merits upon which a finding of *res judicata* could be based. This was argued on the primary basis that the trial testimony of USOA's former counsel had purportedly established that certain alleged remarks of the Referee prior to the signing of his order indicated that the Referee did not intend to dismiss the claim "*with* prejudice." Petitioners admit, however, that the Referee expressly *refused* to state that his order of dismissal was to be "*without* prejudice" (Doc. 33e, pp. 682, 693, 697). Moreover, despite the testimony of USOA's counsel that he had been concerned as to the effect of the Referee's order of dismissal, he admittedly neither reviewed the applicable rule of procedure (Federal Rules 41(b) and (c)) nor made any effort to seek his desired recital in a written form of order submitted to him on the day of, or the day following, the hearing at which the Referee orally expressed his decision to order the dismissal of USOA's counterclaims (Doc. 33e, pp. 639-40; 697-98; Exh. 113e).

In any event, it must be noted here—since petitioners have totally failed to apprise this Court—that subsequent to the opinion of the District Court herein and prior to the affirmance by the Court of Appeals for the Second Circuit, Referee Lipkin had occasion to rule with respect to the intended effect of his own order and has laid to rest any

question concerning his true intentions. Thus, after the Notice of Appeal herein was filed in the Court of Appeals for the Second Circuit (and almost five years after the order of dismissal was entered), USOA, represented by two of the three attorneys for petitioners herein, filed a petition before Referee Lipkin seeking to reform his order of dismissal to reflect that it was intended to be "without prejudice". USOA alleged the very same facts asserted by petitioners in the trial court herein, including the testimony annexed as Appendix B to the Petition for Writ of Certiorari herein.

In a 20-page opinion dated November 15, 1972 and issued while the appeal herein was pending in the Court of Appeals, Referee Lipkin outlined the various events leading up to the dismissal and unequivocally refused to reform his order of dismissal dated August 29, 1967. Thus, Referee Lipkin concluded:

> *There is no basis in fact or law for me to now declare that my Order of August 29, 1967 was without prejudice.* * * *
>
> Aside from the rule of comity that should be applied in this case [referring to the District Court's opinion herein] *I find independently that FRCP 41(b) must be applied, dismissing the counterclaim with prejudice and I further find that the Petitioner is not entitled to any relief under the provisions of FRCP 60(a) and (b).*
>
> I have, with great length, gone into the proceedings before me to clearly indicate that *USOA through Mr. Cox has had the fullest opportunity to prove the facts in other courts namely the State Court and this Court, which he would seek to prove in his suits in the Southern District of New York, and he failed to do so.* That opportunity was available to him as early as June 1966, before Judge Wick in the State Court when he was represented by the same counsel that appeared before me in August, 1967. After the case left the

> State Court and came before me he had all that time for preparation of trial, namely June 1966 to August 1967, and he did not do so. *His conduct was most dilatory though I adjourned the final hearing on the counterclaim before me from May until August when I finally dismissed it.*
>
> This case clearly calls for application, and consistent with the determination of Judge Bauman, of FR [sic] 41(b) and (c) . . . (Exh. Ae, pp. E-20-21) Emphasis added.)*

No petition for review of Referee Lipkin's decision of November 15, 1972 was ever filed and, as indicated above, petitioners do not even acknowledge its existence in their Petition for Writ or Certiorari.

Argument

Further review of the issue presented by the Petition herein is not warranted. The language of Rule 41(b) of the Federal Rules of Civil Procedure unequivocally requires the construction made by the District Court and affirmed by the Court of Appeals that the Referee's order of dismissal was *with* prejudice. Petitioners' argument that the Rule raises only a "rebuttable presumption" is unsupported by any precedent and contrary to the principle that prior orders may not be collaterally attacked by extrinsic evidence. Moreover, petitioners' claim that extrinsic evidence established that the true intention of the Referee was to enter his order *without* prejudice is factually baseless. The Referee who issued the order of dismissal has flatly stated that it was intended to be *with* prejudice. Even in the absence of such a statement, the District Court after hearing all of the extrinsic evidence

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* The state court proceeding referred to in Referee Lipkin's opinion was a proceeding brought by petitioner Cox and USOA seeking to restrain respondent's enforcement of petitioner Cox's guaranty and the sale of USOA's collateral.

offered by petitioners, still found that the order of dismissal was intended to be *with* prejudice. Finally, petitioners' claim that Rule 41(b) "effects a different ultimate result than state law when applied to the same point" (Petition, p. 2) is untrue, is irrelevant by virtue of the Referee's recent opinion, and is untenable in light of the exclusive applicability of the Federal Rules of Civil Procedure in this case.

I

The decision below is clearly correct.

Since Referee Lipkin's order of dismissal was based on a failure to prosecute and was silent with respect to whether it was to be "with" or "without prejudice", the District Court properly held, pursuant to the specific language of Rules 41(b) and (c) of the Federal Rules of Civil Procedure, that the order of dismissal was deemed to be "with prejudice" and therefore constituted an additional basis for imposing the doctrine of *res judicata* against petitioners (Petition, p. 21). The District Court's opinion on this point is supported by a host of prior decisions. See, *e.g., Nasser* v. *Isthmian Lines,* 331 F.2d 124 (2d Cir. 1964); *Kern* v. *Hettinger,* 303 F.2d 333, 339-340 (2d Cir. 1962); *American Nat. Bank & Trust Co. of Chicago* v. *United States,* 142 F.2d 571 (D.C. Cir. 1944); *Perlman* v. *332 West Seventy-Second Street Co.,* 127 F.2d 716 (2d Cir. 1942); *Hicks* v. *Bekins Moving & Storage Co.,* 115 F.2d 406 (9th Cir. 1940); *Fischer* v. *Dover S.S. Co.,* 121 F.Supp. 528 (E.D.N.Y. 1954); *Broder* v. *Hartford Acc. & Indemnity Co.,* 106 F.Supp. 343, 346 (D.D.C. 1952); *Larsen* v. *O'Reilly,* 11 F.R.D. 604 (S.D.N.Y. 1951); *Cf. Weissinger* v. *United States,* 423 F.2d 795 (5th Cir. 1970).

Petitioners have no real basis for disputing the District Court's legal conclusion and thus have cited no case contrary to the above citations. Rather, petitioners argue that

the District Court erroneously "disregarded" certain oral testimony—parol evidence so to speak—that allegedly demonstrated that the order of dismissal was really intended to be "without prejudice". However, there is nothing in the District Court's opinion to indicate that it "disregarded" any testimony or other evidence on this point. The opinion of the District Court clearly sets forth the ultimate facts with respect to the order and the court's legal conclusion (Petition, pp. 19, 21). But even if the District Court had disregarded any such evidence as to what petitioners claim the Referee's "real intentions" were, it is clear that the District Court would have been acting in accordance with the well-accepted rule that a prior order cannot be modified by extrinsic evidence. *American Nat. Bank & Trust Co. of Chicago* v. *United States, supra* at 572; *Kern* v. *Hettinger, supra* at 340; *Weissinger* v. *United States, supra* at 798 ("This sentence [*i.e.*, the last sentence of Rule 41(b)] seeks to avoid 'any need for speculation as to the intent of the court and the effect of its dismissal order where the order fails to indicate whether or not it is with prejudice.' ")

These last-cited cases conclusively refute petitioners' attempt to impose a "rebuttable presumption" test under Rule 41(b) (Petition, p. 11). Significantly, the Petition for Writ of Certiorari does not cite a single decision subsequent to the enactment of Rule 41(b) which supports the "rebuttable presumption" theory.

In any event, if the courts below were to search outside the confines of Referee Lipkin's order of August 28, 1967 for his "real intention", it is submitted that such a search would have to begin, and conclusively end, with Referee Lipkin's own expressions on the matter in his very recent opinion on precisely this subject (Exh. Ae). Thus, as set forth earlier, Referee Lipkin has—ironically upon a "motion for reformation" made by counsel for the petitioners on behalf of USOA—unequivocally stated and independently ruled that his prior order of dismissal was to be

deemed *factually and legally "with prejudice"* (see pp. 6-8, *supra*). Unfortunately, petitioners have failed to apprise this Court of the existence of this opinion, but have obviously failed to do so because standing alone the opinion fully disposes of any contention that the District Court misinterpreted the Referee's order of dismissal.*

However, even in the absence of Referee Lipkin's recent opinion, it is clear that the record herein contains no extrinsic evidence which would lead one to believe that Referee Lipkin intended his order to be "without prejudice". Indeed, based on the fact that defendants' only witness on this point, USOA's former counsel, testified that he had specifically asked Referee Lipkin as to whether the order was to be "with" or "without" prejudice and that Referee Lipkin refused to say it was "without prejudice" and stated only that "it was dismissed" (Doc. 33e, pp. 682, 693 and 697; Exh. Ae, p. E-14); and based on the further fact that USOA's counsel totally failed to review the applicable federal law (Rule 41(b)) or seek a written insertion of the words "without prejudice" in the order, either before or after it was signed (Doc. 33a, pp. 639-640; 697-698), it is clear that the District Court's decision on this issue was neither factually nor legally erroneous. The case of *American Nat. Bank & Trust Co. of Chicago* v. *United States, supra,* is on all fours in this regard.

Petitioners' reliance on some vague colloquy before Referee Lipkin allegedly concerning the availability of respondent for service of process (Petition, p. 5) can hardly have been grounds for the District Court to have departed from the clear language of Rule 41(b). Nor would such a

* Referee Lipkin's opinion has some special additional significance on this appeal because it was rendered (a) in answer to a motion which really constituted an attempt by the present petitioners to collaterally attack the District Court's opinion and (b) in the face of the same testimony—by USOA's former counsel, William P. Doherty, Jr., Esq.—which testimony petitioners claim was disregarded by the District Court.

departure have been warranted merely because USOA's counsel, in his own self-interest and without basis, chose to characterize the order in a letter to petitioner Cox (Exh. 113e) as being "without prejudice" (Petition, pp. 5-6) when, in fact, the order itself was clearly silent on the point and counsel was aware that Referee Lipkin had expressly refused to use those words (Exh. Ae, pp. E-5, 21-22).

Finally, as to petitioners' claim that the District Court should have looked to the law of New Jersey to determine the effect of Referee Lipkin's order of dismissal, it need only be noted that the order of dismissal was rendered in a federal court subject only to the Federal Rules of Civil Procedure (General Order in Bankruptcy 37; 1 Collier in *Bankruptcy*, ¶ 2.81 (14th ed. 1971)); that the order was not rendered in a proceeding based upon diversity jurisdiction; and that the evidence at trial did not even establish that the law of New Jersey was contrary.*

However, even if the procedural rules of New Jersey were contrary to the Federal Rules of Civil Procedure, the District Court properly applied Rule 41(b) regardless of its effect upon the outcome of the litigation. See, *e.g.*, *Hanna* v. *Plumer*, 380 U.S. 460, 468-70 ("The Erie rule has never been invoked to void a Federal Rule."). Thus, in *Kern* v. *Hettinger*, *supra*, the Second Circuit squarely rejected the contention that a district court sitting in a diversity action was required to follow the California law and hold that another federal court's order of dismissal for lack of prosecution was (unlike Rule 41(b)) without prejudice to a subsequent action:

> "It would be destructive of the basic principles of the Federal Rules of Civil Procedure to say that the effect

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* In fact, contrary to petitioners' assertion, under the New Jersey rules of procedure, an involuntary dismissal for failure to prosecute, like Rule 41(b), apparently operates as an adjudication on the merits unless the order of dismissal specifies otherwise. See New Jersey Civil Rule § 4:37-2(d) (Eff. September 8, 1969); Id., § 4-42-2(b) (Eff. September 9, 1953); Id., § 1:2-4.

> of a judgment of a federal court was governed by the law of the state where the court sits simply because the source of federal jurisdiction is diversity * * *. [W]e think it would be strange doctrine to allow a state to nullify the judgments of federal courts constitutionally established and given power also to enforce state created rights. The Erie doctrine, [Erie R. Co. v. Tompkins, 304 U.S. 64 * * *] is not applicable here * * *." 303 F.2d at 340.

Indeed, in *Byrd* v. *Blue Ridge Rural Electric Cooperative, Inc.*, 356 U.S. 525—inexplicably relied upon by petitioners—this Court held that in a diversity action the federal court was *not* bound by the state law's limitation of the issues submitted to the jury, even though the absence of such a limitation might change the outcome of the suit. Of course, where the first court's jurisdiction is predicated not upon diversity but federal law (*i.e.*, the Bankruptcy Act), the considerations governing the Erie doctrine—forum-shopping and the inequitable administration of the laws—are absent, and there is no reason to interpret its order in accordance with state law. *Cf. Hanna* v. *Plumer*, *supra*, at 467-48.

II

The petition does not raise any issue requiring review by this Court.

Petitioners do not claim that the decision below is in conflict with any other decision construing Rule 41(b), nor do they claim that the language of that statute is ambiguous. To the extent that petitioners attempt to create an *Erie R. Co.* v. *Tompkins* issue because an allegedly different New Jersey rule of procedure would have been "outcome determinative", they are raising an issue which is factually unsupported and which in any event has been unanimously decided against them by this Court in *Hanna*

v. *Plumer, supra.* The adoption of petitioners' argument would undermine the uniform application of the Federal Rules of Civil Procedure and, if carried to its logical conclusion, would replace the Federal Rules with a different code of procedure for each state. It is ironic that petitioners should urge such a radical departure from the well-settled law in a case where, even if their position was adopted, the ruling below would not be disturbed because the very court which entered the order has stated that it in fact intended to dismiss *with* prejudice.

The mandate of the statute is clear, and the application of that statute by the courts below was both factually and legally correct. Further consideration of the issue presented by the Petition for Writ of Certiorari would not serve the interests of the courts, other litigants, or even the petitioners herein. There is no issue raised herein which is worthy of review by this Court, and the Petition for Writ of Certiorari should be denied.

CONCLUSION

For the foregoing reasons it is respectfully submitted that this Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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